

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)	
)	
Cost Review Proceeding for Residential and)	CC Docket No. 96-262
Single-Line Business Subscriber Line Charge)	
(SLC) Caps)	
)	
Access Charge Reform)	CC Docket No. 94-1
)	
)	
Federal-State Joint Board on Universal Service)	CC Docket No. 96-45

COMMENTS OF SPRINT CORPORATION

Sprint Corporation hereby files its reply to comments filed on cost studies submitted by incumbent local exchange carriers in the above-captioned proceeding.¹ Significantly, none of the comments filed disputed Sprint's conclusion that its costs far exceed the SLC cap and that the scheduled increase in the residential SLC cap above \$5.00 is cost justified. The single issue raised specific to Sprint's cost submission was an assertion by the National Association of State Utility Consumer Advocates (NASUCA) that Sprint incorrectly assigned common costs to the loop. This assertion is without basis. Sprint's cost demonstration was based entirely on the FCC's Delphi version of the HCPM (in its default form), including the model's (not Sprint's) methodology for

¹ *In the Matter of Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers*, CC Docket Nos. 96-262 and 94-1, *Sixth Report and Order, Low-Volume Long-Distance Users*, CC Docket No. 99-249, *Report and Order, Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Eleventh Report and Order*, 15 FCC Rcd 12962 ("CALLS Order"), aff'd in part, rev'd in part, and remanded in part, *Texas Office of Public Util. Counsel et al. V. FCC*, 5th Cir. Nos. 00-60434 (5th Cir. September 10, 2001).

allocating common costs. Even if Sprint had stepped outside the FCC's model and allocated the common cost across all elements, as NASUCA suggested, the impact that such an allocation might have had on Sprint's filing would have been negligible and inconsequential with respect to justification for the SLC cap increase.

Sprint disagrees with various other assertions made by NASUCA, which, while not directed toward Sprint's cost submission, represent inappropriate costing principles and methodologies. NASUCA erroneously states that the total element long run incremental cost (TELRIC) standard should be used in setting SLC prices and challenges the use of company-specific data in evaluating cost for SLC cap purposes. NASUCA also proposes that, because loops are used in the provision of advanced services, a portion of the loop cost should be allocated to those services. None of these assertions has merit. The only reasonable method for calculating company-specific cost, particularly for the purpose of evaluating appropriate company-specific prices, is through company-specific inputs. The notion that loop costs should be allocated away from the loop is a tired, well-worn, but settled debate that has no place in this proceeding. Finally, Sprint supports comments filed by the General Services Administration (GSA), stating that cost submissions that average the cost of providing residential lines with the cost of providing business lines understate the cost of providing residential lines alone. Thus, submissions by carriers such as Sprint who demonstrate in their submission that their costs exceed the scheduled SLC caps even when presented as an average that understates residential line costs, clearly establish justification for the SLC cap increase.

I. NASUCA’S COMMON COST CLAIM IS FLAWED

In its Comments, NASUCA erroneously challenges Sprint’s cost study, stating that Sprint “incorrectly assigned 100% of common costs to the loop.”² Contrary to NASUCA’s assertion, common costs were assigned by the Commission’s cost model, not by Sprint. As Sprint clearly stated in its cost submission, it calculated its costs using the Commission’s cost model, the Delphi version of the Synthesis Model (HCPM) in its default form. Sprint further explained that it used the Commission’s model rather than submitting its own model in an effort to minimize the amount of time and resources expended in preparing its cost submission. The HCPM allocates all of the common cost (“Per Line cost”) to the network interface device (NID), rather than allocating the common cost across all elements.

Furthermore, since the common cost input used by the model excludes common costs attributable to services that are not supported by the federal universal service support mechanism,³ NASUCA’s assertion that 100% of common costs were assigned to the loop is incorrect. Also, since the SLC represents recovery of just the interstate portion of line costs, Sprint applied a 25% factor to the unseparated model results, including unseparated common cost. Therefore, less than 25% of common costs, not 100% as asserted by NASUCA, were assigned to the SLC.

² NASUCA comments at 29.

³ *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45; *Forward-Looking Mechanism for High Cost Support for Non-Rural LECs*, CC 97-160, *Tenth Report and Order* (rel. Nov. 2, 1999) at 164-165. The Commission explained that: “The specifications used were designed to separate the portion of expenses attributable to special access and toll usage, which are not supported by the federal high-cost mechanism, from the portion of expenses attributable to switched lines and local usage, which are supported.”

Most importantly, even if Sprint had acted beyond the confines of the HCPM, and allocated the FCC's default common cost per line across all elements, the impact on the cost results would have been negligible, and the SLC cap increase would still be justified. In states in which Sprint provides local service, the loop and port cost combined comprise approximately 90 percent of the total cost of service before common cost is applied. This difference between the HCPM's 100% allocation and a 90% allocation is even smaller considering that the SLC represents only the interstate portion, or 25%, of loop and port cost, amounting to a mere 2.5% difference. Given the model's common cost per line of \$7.32, the difference in allocation would be eighteen cents per line ($\$7.32 \times 2.5\% = \0.183). Sprint's submission demonstrated that its costs exceed the scheduled SLC cap by a much larger amount. Thus, NASUCA's challenge to Sprint's allocation of common costs "to the loop" is without merit.

II. OTHER MATTERS

A. *TELRIC for Retail*

NASUCA's comments suggest that total element long-run incremental cost (TELRIC) be used as the standard for setting SLCs.⁴ However, in taking this position, NASUCA demonstrates its confusion regarding three key facts: 1) the pricing standards for unbundled elements and interconnection established by the Commission serve a unique purpose with regard to the entry of competitors; 2) by using economic cost at the

⁴ NASUCA Comments at 8. Sprint notes that the pricing standard established by the Commission for unbundled elements ("UNEs") is *economic cost*, not TELRIC. Economic cost consists of an incremental portion (TELRIC) plus an addition that represents a contribution to the firm's joint and common costs. See

wholesale level, the Commission has encouraged the use of competition—as opposed to regulatory mandate—as the controlling factor on prices at the retail level, which ultimately serves the consumer best; and 3) the Commission has never advocated or required setting the retail, end-user price for basic local service equal to economic cost (or TELRIC).

The 1996 Act required incumbent providers to make their network elements available because potential competitors lack the economies of scale built into the existing public switched telephone network. Although true facilities-based competition has always been one of the Commission’s goals, it is probable that, in many areas, competitors would find it economically infeasible to replicate the entire network, or even significant portions of it. Therefore, successful competition was (and is) dependent on allowing competitors the choice of entering a market by building their own facilities or by leasing the incumbent’s facilities. By basing UNE prices on forward-looking economic costs, the correct signal is sent for competitive facilities based entry. If UNE prices were based on historical costs and, in certain cases, historical costs exceeded forward-looking costs, potential entrants could make the decision to build even though the reality was such that they could not do so more efficiently than the incumbent. As the Commission stated, forward-looking costs should be used “in order to encourage efficient levels of investment and entry.”⁵

In the case of retail services such as basic local service, the consumer is best served by allowing market forces and competition to operate unencumbered as controlling factors on prices. The use of TELRIC-based economic costs in the wholesale

Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, First Report and Order, CC Docket No. 96-98 (rel. Aug. 8, 1996) (“First Report and Order”) at 329-332.

market, which allows for competitive entry where it might not otherwise occur, is a means toward this end. However, NASUCA appears to advocate the instantaneous imposition of TELRIC-based, economic cost as some type of price ceiling for retail services. Such an action interferes with the market/price mechanism. It is true that competition does drive end-user prices toward costs, actual costs. Competition does drive actual costs toward their most efficient level, which are economic costs. But these economic costs may or may not be equivalent to the values NASUCA believes are correct. If any of the assumptions or calculations contained in NASUCA's cost estimates proves incorrect, the resulting prices would thwart competition. NASUCA's assertion that the Commission set retail rates at TELRIC should be rejected.

B. Company-specific Inputs

NASUCA opposes the use of company-specific data in evaluating LECs' costs,⁶ however company-specific inputs are the appropriate means for evaluating company-specific costs, and particularly for evaluating company-specific rate levels. As Sprint has stated in the past, nationwide, default proxy cost inputs do not accurately depict the costs of an efficient company the size of Sprint providing service in Sprint's operating territories. Only company-specific, forward-looking cost inputs accurately reflect such costs.

Sprint actively participated in the Commission's input workshops and the input development process as a whole, and it is Sprint's understanding that the Commission at

⁵ First Report and Order at 328.

⁶ NASUCA Comments at 20.

no time intended to develop inputs that might be used for UNE costing or retail pricing.⁷ Furthermore, as Sprint pointed out in its cost submission, the Commission has acknowledged that the Synthesis model was solely applicable to universal service, stating: “For universal service purposes, we find that using nationwide averages is appropriate. The Commission has not considered what type of input values, company-specific or nationwide, nor what specific input values, would be appropriate for any other purposes....It may not be appropriate to use nationwide values for other purposes, such as determining prices for unbundled network elements. We caution parties from making any claims in other proceedings based upon the input values we adopt in this Order.”⁸ In summary, NASUCA’s objection to using company specific inputs is misguided. There is a huge difference between determining which areas of the nation are high cost areas relative to other areas of the nation and determining a specific company’s costs for the purpose of setting that company’s rates. NASUCA’s assertion that the cost inputs used for the first exercise are readily transferable to any other exercise should be rejected.

C. Allocating Loop Costs to Advanced Services

NASUCA’s comments erroneously propose that because loops are used in the provision of advanced services such as XDSL, a portion of the loop cost should be allocated to those services. On a very obvious level, this argument is nothing more than a tired attempt to perpetuate an old controversy regarding allocation of loop costs across multiple services that has long since been settled. As Dr. Alfred Kahn succinctly stated, testifying on this subject before the Pennsylvania Public Utility Commission:

⁷ *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45; *Forward-Looking Mechanism for High Cost Support for Non-Rural LECs*, CC Docket No. 97-160, Further Notice of Proposed Rulemaking, FCC 99-119 (rel. May 28, 1999), Comments of Sprint Corporation at 4.

⁸ Input Order

“The arguments proffered by these witnesses [that the loop is a shared cost] are the most persistent weeds in the regulatory garden. Other mainstream economists and I have dealt with and debunked these claims for years—and I suppose this will remain our task for as long as parties to proceedings such as this insist on conflating the politics of setting prices with the economics of determining costs.”⁹

Sprint will not reiterate arguments in the long-standing debate here. Rather, below we address the clearly *de minimis* effect that any such (economically unjustified) adjustment would have.

If in fact a portion of loop costs was (erroneously) allocated to advanced services it is extremely unlikely that such an allocation would have any measurable effect on the costs provided in this docket. According to the FCC’s most recent data provided in its Third Report on Advanced Services, CC Docket 98-146, released February 6, 2002 (“Third Report”), wireline advanced service penetration of telephony-based services is approximately 2.006%.¹⁰ As a result, even if an ill-conceived “adjustment” were made assigning a portion of loop costs to the small minority of advanced service subscribers, the difference in the cost of the remaining vast majority of loops not used for advanced services would be negligible. Line costs would still exceed the scheduled SLC caps, and the increase in SLC caps would still be justified.

An assignment of loop costs to advanced services is merely the latest effort in a long history of political price rigging that has been soundly refuted by the mainstream economists and enlightened policy makers. Also, given the small level of advanced

⁹ Rebuttal testimony of Dr. Alfred Kahn before the Pennsylvania Public Utility Commission, Docket No. I-940035, February 15, 1996. An excellent overview of this debate can be found in “*Seven Years After Kahn and Shew: Linger Myths on Costs and Pricing Telephone Service*,” Steven Parsons, PHD, Yale Journal on Regulation (1994). This article provides a thorough discussion of this topic and demonstrates that Dr. David Gabel, one of the co-authors of NASUCA’s comments, is a longtime advocate of the contrary opinion.

¹⁰ According to the FCC’s Third Report, there are 3,781,900 ADSL and other wireline high-speed lines offering at least 200 kbps in at least one direction. Using NECA data on total wireline lines nationwide for

services penetration, a misguided attempt to assign away loop costs to the small base of customers of advanced services would have essentially no impact on the loop costs of the vast remaining majority. Finally, an assignment of loop costs to advanced services is clearly outside the scope of this proceeding.

III. AVERAGING THE COST OF RESIDENTIAL AND BUSINESS LINES UNDERSTATES RESIDENTIAL COST

Sprint agrees with GSA's observation that cost submissions that average the cost of providing residential lines with the cost of providing business lines understate the cost of providing residential lines alone. This is true because business lines tend to be located in areas of higher line-density than residential areas. Sprint's submission provided average cost results without distinguishing between residential and business lines and therefore understated residential-only costs just as GSA suggests. Given that Sprint's submission demonstrated that its costs exceeded the scheduled SLC caps even when presented as an average that understates Sprint's residential line costs, the Commission can rest assured that the residential SLC cap increase is well justified.

Year End 2000 of approximately 188,485,132 wireline lines, this produces a telephony-based advanced service penetration rate of 2.006%.

IV. CONCLUSION

For the foregoing reasons, Sprint urges the Commission to accept Sprint's cost submission as fully justifying the scheduled SLC cap increase.

Respectfully submitted,

Sprint Corporation

By: /s/

Jay C. Keithley
Rikke K. Davis
401 9th Street, NW
Washington, DC 20004
(202) 585-1920

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Its Attorneys

CERTIFICATE OF SERVICE

I, Joyce Y. Walker, hereby certify that I have on this 14th day February 2002, served via U.S. First Class Mail, postage prepaid, or Hand Delivery, a copy of the foregoing comments," In the Matter of Access Charge Reform, CC Docket No. 96-262, and Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, with the Secretary, Federal Communications Commission, to the persons listed below.

//s//

Joyce Y. Walker

**Tamara Preiss
Federal Communications
Commission
445 12th Street SW.,
Washington, DC 20554**

**Gary M. Choen
Lionel B. Wilson
Ellen S. Levine
Attorneys for the People of the State of
California
And the California Public Utilities
Commission
505 Van Ness Avenue
San Francisco, CA 94102**

**Qualex International
Federal Communications
Commission
445 12th Street SW
Washington, DC 20554**

**George N. Barclay
Michael J. Ettner
General Services Administration
1800 F Street NW., Room 4002
Washington, DC 20405**

**Michael J. Travieso
Maryland People Counsel
6 St. Paul Street, Suite 2102
Baltimore, MD 21202**

**Alan Buzacott
WorldCom, Inc.
1133 19th Street NW
Washington, DC 20036**

**Steven C. Emmanuel
Kent R. Spuhler
Florida Legal Services, Inc.
2121 Delta Blvd
Tallahassee, FL 32303**

**Kevin S DiLallo
James S. Blaszak
Levine, Blaszak, Black & Boothby, LLP
Counsel for Ad Hoc Telecommunications
Users Committee
2001 L Street N.W., Suite 900
Washington, DC 20036**

**Joel Ader
Telecordia Technologies
710 L'Enfant Plaza S.W.,
Promenade Level, East Building
Washington, D.C. 20024**